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6 **IN THE UNITED STATES BANKRUPTCY COURT**

7 **FOR THE DISTRICT OF ARIZONA**

9 In re:

10 CHARLES THOMAS BROWN d/b/a TOM  
11 BROWN PREFERRED TRUST COMPANY,

12 Debtor.

13 MAUREEN GAUGHAN, Chapter 7 Trustee

14 Plaintiff,

15 v.

16 ANN AKAMINE, et al.,

17 Defendants.

Proceedings Under Chapter 7

No. B97-14228 PHX GBN

Adv. 99-746

**TRUSTEE'S RESPONSE TO PATRICK  
O'CONNOR'S MOTION TO ALTER OR  
AMEND JUDGMENT AND FOR NEW  
TRIAL**

[No hearing set at this time]

18 This Court has granted (1) Final Judgment against Patrick O'Connor in favor of Maureen  
19 Gaughan, the Chapter 7 Trustee ("Trustee") on certain preferential transfers and (2) partial summary  
20 judgment against Mr. O'Connor on the Trustee's fraudulent conveyance claims against him. Mr. O'Connor  
21 has filed his Motion to Alter or Amend Judgment and for New Trial ("Motion"), asking the Court to  
22 reconsider its decision. For the reasons set forth below, the Trustee asks the Court to deny Mr. O'Connor's  
23 Motion and to award her attorneys' fees and costs.

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1 **PARTIAL SUMMARY JUDGMENT ON FRAUDULENT PREFERENCE CLAIM WAS APPROPRIATE**

2 Mr. O'Connor argues that the Court's grant of partial summary judgment on the fraudulent  
3 transfer claims cuts off potential defenses that the Trustee represented to the Court would be preserved.  
4 Mr. O'Connor supports his argument by confusing three separate provisions of Arizona's fraudulent transfer  
5 law, A.R.S. §§ 44-1004.A 1, 44-1004.B.8 and 44-1008.A. Once these sections are untangled, it is obvious  
6 that the Court's entry of partial summary judgment was appropriate.

7 The Arizona legislature has adopted certain indicia of fraud that can assist a litigant in proving  
8 actual fraud. Those non-exclusive indicia are set forth in A.R.S. § 44-1004.B and include, as one example,  
9 whether reasonably equivalent value was exchanged for the transfer. The Court need not address whether  
10 there is a disputed factual issue over whether one of the indicia of fraud is present under subsection B, if the  
11 Court finds that Mr. Brown made the transfer with the actual intent to hinder, delay and defraud under A.R.S.  
12 § 44-1004.A.1. In this case, the clear and uncontroverted evidence of Mr. Brown's Ponzi scheme establishes  
13 Brown's actual intent sufficient to support the Court's grant of partial summary judgment under controlling  
14 Ninth Circuit case law. Mr. O'Connor has not submitted any evidence or arguments that raise a factual issue  
15 as to whether Mr. Brown was operating a Ponzi scheme. Moreover, although the transfers have been  
16 deemed fraudulent, Mr. O'Connor may still argue that the fraudulent transfers to him should not be avoided  
17 under A.R.S. § 1008.A if he took the transfers in good faith and for reasonably equivalent value.  
18 Accordingly, Mr. O'Connor's potential defense has been preserved and his Motion should be denied.

19 **CLAIM WAS PROPERLY DISALLOWED**

20 Mr. O'Connor argues that his claim should not be disallowed in its entirety. Section 502(d)  
21 of the Bankruptcy Code provides that the Court shall disallow the claim of any entity from which property  
22 is recoverable or that is a transferee of a transfer avoidable under various sections of the Bankruptcy Code  
23 unless such transferee has paid the amount, or turned over any such property, for which such entity or  
24 transferee is liable. In this case, the Court has entered a final judgment against Mr. O'Connor that he is liable  
25 to the Trustee for a preferential transfer in the amount of \$37,800.00, plus interest. Mr. O'Connor has not  
26 paid this amount and accordingly, his claim is appropriately disallowed. If, in the future, Mr. O'Connor pays

1 this amount (and any additional amount that the Court may award to the Trustee under her fraudulent transfer  
2 claims), then his claim may be allowed either by stipulation with the Trustee or by seeking relief from the  
3 Court. Bankruptcy Rule 3008, which governs the reconsideration of allowance of claims, provides no time  
4 limit within which a party may ask the Court to reconsider the allowance of a claim. Accordingly, disallowing  
5 the claim was appropriate and Mr. O'Connor's objection should be overruled.

6 **ORDINARY COURSE OF BUSINESS DEFENSE DOES NOT APPLY**

7 Mr. O'Connor argues that the Court should reconsider its decision because the transfer to  
8 Mr. O'Connor was made within the ordinary course of business exception found in § 547(c)(2)(A) of the  
9 Bankruptcy Code.<sup>1/</sup> In the response, Mr. O'Connor acknowledges that the Ninth Circuit case law holding  
10 that the ordinary course of business exception is not available in a Ponzi scheme case. *See, In re Bullion*  
11 *Reserve of North America*, 836 F.2d, 1214 (9<sup>th</sup> Cir. 1988), *cert. denied*, 108 S.Ct. 2824, 100 L.Ed. 2d 925  
12 (1988). Mr. O'Connor attempts to distinguish the controlling authority of *Bullion Reserve* by relying upon  
13 Judge Bilby's decision in *In Re American Continental Corp.*, 142 B.R. 894, 900 (D.Az 1992). In that case,  
14 although the debtor argued that the case involved a Ponzi scheme, Judge Bilby held that individuals who had  
15 received payments on certain bonds purchased at Lincoln Savings were entitled to assert an ordinary course  
16 of business defense to a preference claim.

17 In *American Continental*, Judge Bilby relied upon the then recent decision of *United Bank*  
18 *v. Wolas*, 502 U.S. 151, 112, S. Ct. 527, 116 L.Ed. 2d 514 (1991), to distinguish the otherwise controlling  
19 case of *Bullion Reserve*. In *Wolas*, the Supreme Court overruled the Ninth Circuit to find that payments on

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25 <sup>1/</sup> Even if the Court were to consider Mr. O'Connor's legal arguments, Mr. O'Connor has not  
26 submitted any facts to establish his burden that his transfers were in the ordinary course of business. He has  
not presented an affidavit or other evidence to support his defense. Accordingly, the Court should deny his  
Motion.

1 a long-term debt could qualify for the ordinary course of business defense to a preference claim. *Wolas* did  
2 not involve a Ponzi scheme case and its application in *American Continental*. was questionable.<sup>2/</sup>

3 Since *American Continental* was decided, the Ninth Circuit has had occasion to revisit the  
4 issue in *Henderson v. Buchanan*, 985 F.2d 1021 (9<sup>th</sup> Cir. 1993) and has reaffirmed its earlier decisions that  
5 a payment to an investor in a Ponzi scheme does not qualify as a payment in the ordinary course of business  
6 for purposes of a defense to a preference payment. Subsequent case law makes clear that the ordinary course  
7 of business defense simply is inapplicable to a payment to an investor in a Ponzi scheme because either the  
8 exception does not apply to illegitimate businesses or the debt and the transfers are not made according to  
9 ordinary business terms. See, *Jobin v. McKay (In Re M&L Bus. Mach. Co.*, 84 F.3d 1330 (10<sup>th</sup> Cir. 1996);  
10 *In Re Rodriquez*, 209 B.R. 424 (Bankr. S.D. Tex 1997); *In Re National Liquidators Inc.*, 232 B.R. 915  
11 (Bankr. S.D. Ohio 1998); *Pajaro Dunes Rental Agency v. Spitters*, 174 B.R. 557 (Bankr. N.D. Cal. 1994)).  
12 The Trustee asks the Court to overrule Mr. O'Connor's Motion for reconsideration of the judgment on the  
13 preference claim.

#### 14 **REQUEST FOR ATTORNEY FEES**

15 The Trustee has been forced to incur additional attorneys' fees in responding to  
16 Mr. O'Connor's Motion. These fees diminish the ultimate return to unsecured creditors in the case. The

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23 <sup>2/</sup> In the *American Continental* case, Judge Bilby specifically indicated that he based his  
24 decision on the "equities." Obviously, he was troubled by the suit against numerous individuals who had lost  
25 significant sums of money in what they believed were federally insured deposits. These "equities" --however  
26 strong a court might find them -- are not sufficient reason to ignore the standing and controlling Ninth Circuit  
precedent. The Supreme Court has repeatedly reigned in courts from exercising vague notions of equity in  
interpreting the Bankruptcy Code. Moreover, it is unclear why it is more equitable to allow a preference  
defendant who received a return of money immediately before bankruptcy to retain these funds as against  
other equally deserving investors.

1 Trustee requests that the Court award her reasonable attorneys' fees and costs incurred in responding to the  
2 Motion.

3 DATED this \_\_\_\_\_ day of January, 2001.

4 **RYLEY, CARLOCK & APPLEWHITE, P.A.**

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7 By:/s/ John J. Fries - 007182  
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10 Phoenix, AZ 85003-1973  
11 Attorneys for Maureen Gaughan, Chapter 7  
12 Trustee

11 **Copies** of the foregoing mailed this  
12 16th day of January, 2001 to:

13 Randy Nussbaum  
14 Jaburg & Wilk, P.C.  
15 3200 N. Central Avenue  
16 Phoenix, AZ 85012

17 UNITED STATES TRUSTEE'S OFFICE  
18 P.O. Box 36170  
19 Phoenix, Arizona 85067-6170

20 By:/s/ Deborah Robertson  
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